16 C.F.R. Part 310: Telemarketing Sales Rule
Notice of Proposed Rulemaking to Amend the Rule
To Address the Sale of Debt Relief Services,
and Announcement of Public Forum
Summary of Communications Pursuant to Commission Rule 1.26(b)(5)

Donald S. Clark
Secretary
June 30, 2010

MEMORANDUM

To: Don Clark
From: Carolyn L. Hann, Attorney Advisor, Office of Commissioner J. Thomas Rosch
Re: Telemarketing Sales Rule – Debt Relief Amendments, Comments to Be Placed on the Public Record
Date: June 30, 2010

On Monday, June 28, 2010, representatives from the Attorney General offices of Illinois, North Carolina, and Texas participated in a telephone conference with FTC Commissioner Rosch, his attorney advisor, and FTC staff members to discuss the proposed debt relief amendments to the Telemarketing Sales Rule.[1]

The representatives expressed strong support for the proposed amendments, especially the prohibition on advance fees, which they view as the "cornerstone" of the proposal.

The North Carolina representative stated that North Carolina law has prohibited the collection of advance fees by debt relief servicers since 2005. He further stated that he has spoken with a number of debt settlement companies. He asserted that some of these companies do not charge up front fees, yet they can do - and in fact are doing - business in North Carolina. He noted that this stands in contrast to arguments by industry that it could not survive under an advance fee ban.

A Texas representative said that they have six cases against debt settlement companies in pending litigation. He asserted that the consumers in these cases make payments to the companies for several months (not realizing that most of the payments go towards fees, rather than settlement offers), then face lawsuits (from creditors and debt collectors), which forces them to drop out of the programs. He further asserted it is only at that point that the consumers realize the fees are non-refundable. He further stated that the alleged conduct in these cases mirrors the conduct described in the NAAG comments (dated Oct. 23, 2009) submitted for the rulemaking record.

An Illinois representative stated that the state has filed seven lawsuits against debt settlement companies, including members of The Association of Settlement Companies ("TASC") and the United States Organization for Bankruptcy Alternatives ("USOBA"). For that reason, the representative stated that she sees no distinction between conduct by debt settlement companies who are not affiliated with a trade association, and those who are members of one. She further asserted that there are widespread deceptive practices in the industry, and that she is

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[1]Participating from the office of the Illinois Attorney General were: Deborah Hagan, Elizabeth Blackston, and Rebecca Pruitt. Participating from the office of the North Carolina Attorney General was: Philip Lehman. Participating from the office of the Texas Attorney General were: Esther Chavez and Paul Singer.

In attendance from the FTC were: Commissioner Rosch, Carolyn Hann, Lawrence DeMille-Wagman, and Allison Brown.

hard-pressed to find cases where consumers have received net tangible benefits from debt relief services.

Another Illinois representative described new state legislation that was passed by the Illinois legislature. The law bans advanced fees, caps fees at 15% of the savings achieved (a "success fee") if debts are settled, and allows the companies to charge small sign-up fees. This representative also said that at the legislature's hearing for this law, one consumer witness testified that his/her debt settlement company did not settle any of this consumer's debts. The representative further stated that another consumer witness paid $2 in fees for every $1 saved from debts successfully settled by a debt settlement company.

A third Illinois representative stated that the Illinois AG's office has had frequent discussions with Chase Bank. According to this state representative, Chase Bank refuses to negotiate with any debt settlement companies. Since Chase Bank is one of the biggest creditors for consumers, this representative surmises that debt settlement provides no benefit for many consumers.

An Illinois representative stated that industry members claim they will go out of business under an advance fee ban regime. However, this representative said that one small debt settlement company met with the Illinois AG's office and stated that it could operate on a fee-per-settled debt ("pay for performance") basis. In addition, another debt settlement company located in Arizona told the Illinois AG's office that it could operate without receiving advance fees.

An Illinois representative questioned the fundamental value of debt settlement services if creditors will not cooperate, the cost of the fees exceeds the amount of savings, the consumer still risks being sued by creditors, and incurs harm to his or her creditworthiness. This representative reiterated that the advance fee ban is the "lynchpin" of the proposed amendments to the FTC's rule because such ban would enable consumers to save money towards settlement.

An Illinois representative stated that an U.S. Bankruptcy Trustee located in Illinois expressed grave concerns about the number of consumers filing for bankruptcy who previously paid a lot of fees to debt settlement companies.

Commissioner Rosch asked a few questions. First, he asked about the mechanics of the advance fee ban that the representatives were endorsing: it is to prohibit servicers from collecting fees until all debts are settled, or letting them collect fees proportional to each debt settled? An Illinois representative stated that they are supportive of a per-debt settled basis, not requiring the servicers to wait until all debts are settled. The North Carolina representative stated that the North Carolina law allows the servicer to do either (collect fees per debt settled or for total debts settled). A Texas representative stated that its position is reflected in the NAAG comments; that is, the concern is collecting fees before providing any services. The Texas representative further stated that they have no objection to collection of a fee per debt settled.

Second, Commissioner Rosch asked, based on the NAAG comments, what is the most

powerful evidence that advance fees are abusive or undesirable? The North Carolina representative stated that consumers pay fees, receive no services, and drop out – and that is fundamentally unfair. An Illinois representative stated that while there are many factors, the drop-out rate is probably the biggest concern. A Texas representative stated that consumers do not appear to benefit from these services. For example, in a lawsuit against one debt settlement company, 80% of consumers never got any debts settled. In addition, the Texas representative asserted that there is a lack of any statistics or data from industry demonstrating that consumers benefit from these programs.

Third, Commissioner Rosch asked whether the representatives know why the drop-out rate is what it is or why consumers drop out? For example, did the representatives have any statistics? One Illinois representative stated that their drop-out information was obtained anecdotally, not based on statistics. Another Illinois representative cited a white paper by Richard Briesch, PhD.[2] The representative described the white paper as demonstrating that 60% of consumers cancel within two years, and that consumers start to complain about their services approximately six to 12 months into their program. A Texas representative referred to the TASC 2008 Preliminary Survey attached to the NAAG Comments, describing the survey as showing program completion rates of 35-60%, where "completion" means at least half of all accounts were settled.

Fourth, Commissioner Rosch asked whether we would be doing consumers any favors by driving them into the hands of creditors such as Chase Bank (rather than seeking debt settlement services). An Illinois representative asserted that of all the options available to a debtor, debt settlement is the worst: it aggravates the problem rather than solving it. In some cases, non-profit credit counseling is better; in other cases, bankruptcy is better. The Illinois representative expressed belief that Chase Bank would try to work with borrowers. However, she conceded that she did not have any statistics on how effective Chase Bank is in dealing directly with debtors.

Fifth, Commissioner Rosch noted that the proposed debt relief amendments are part of the Telemarketing Sales Rule. Thus, he asked what would prevent industry from moving to a different model, say door to door sales and charging advance fees? An Illinois representative surmised that industry always manages to find the next way to get around rules. However, she noted that it would be hard for these companies to avoid telemarketing.

Sixth, Commissioner Rosch asked about the coverage of the Illinois statute. He first asked whether it is limited to telemarketing and second, how the legislature determined the 15% fee cap. As to the first part of the question, an Illinois representative stated that the Illinois statute applies regardless of the method of solicitation (e.g., telemarketing, door-to-door). In

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[2]Economic Factors and the Debt Management Industry," Richard A. Briesch, PhD, Associate Professor, Southern Methodist University, August 6, 2009, at 12, available at http://www.consumercreditchoice.org, attached to the comment submitted to the rulemaking record by the J. Hass Group, Oct. 24, 2009.

addition, the statute allows the consumer to cancel at any time, and to be returned any unearned fees. As to the second part of the question, the Illinois representative stated that they do not have actual statistics for determining the 15% fee cap. However, they thought 15% represented a fairly large percentage. Another Illinois representative added that under the Illinois statute, in addition to being eligible for up to 15% of the savings achieved, the company also could charge an enrollment fee as well as a back-end fee.

A FTC representative asked the state representatives how they selected the cases that became the subject of law enforcement action. An Illinois representative stated that their defendant companies had more consumer complaints than other companies, but were not outliers in the industry. She also noted that many of the defendants are members of trade associations. A Texas representative stated that many of the cases name TASC or USOBA members and that the allegations in these cases are largely similar. Representatives of both states said that they have seen many other debt settlement companies engaging in illegal practices, but they don't have the resources to conduct full investigations of all of them.

A FTC representative asked the North Carolina representative whether he has noticed a decline in the number of debt settlement companies operating in North Carolina as a result of the advance fee ban in its law. The North Carolina representative stated that yes, many debt settlement companies have moved out of North Carolina, presumably due to the ban.

A FTC representative asked whether any of the state representatives were aware of debt relief services being offered over Skype or other telephone-type Internet programs. None of the representatives were aware of any such trend.

A Texas representative added that many auto warranty and credit card interest rate reduction telemarketers are shifting to debt settlement, since law enforcement actions have increased in the former two areas. One of the state representatives surmised that debt settlement is the new incarnation of these large fee scams.